Central Intelligence Agency

Washington, D.C. 20505

DIRECTORATE OF INTELLIGENCE

10 February 1988

Vietnam: Banking on New Law To Attract Western Investors

Summary

Vietnam's new foreign investment law, aimed at attracting badly needed Western capital and technical expertise, is, we believe, unlikely to live up to Hanoi's high expectations. Vietnam's weak infrastructure, primitive banking system, and stifling bureaucracy will continue to discourage foreign investors. Furthermore, the law has no effect on the major stumbling block to Western assistance, the presence of Vietnamese troops in Cambodia. It is clear, though, that Hanoi is using its new investment code and growing international interest in possible commercial opportunities in Vietnam to try to break out of its economic isolation even while its troops remain in Cambodia. [redacted] 25X1

This memorandum was prepared by [redacted] Office of East Asian Analysis. 25X1
Information available as of 8 February 1988 was used in its preparation. Comments and queries are welcome and may be directed to the Chief, Indochina, Thailand, and Malaysia, Southeast Asia Division, OEA, [redacted] 25X1

EA M 88-20010

[redacted] [redacted] 25X1
25X1

[redacted] 25X1

Historical Perspective

Vietnam's National Assembly passed a foreign investment code at the end of 1987 to lure Western assistance for its ailing economy (see Appendix A). Hanoi is counting on foreign investment to provide the new equipment, spare parts, and managerial expertise needed to upgrade its antiquated factories. Adoption of the code, which was delayed for three years by lengthy debates between reformists and conservative party members, caps a year of capitalist-style reforms introduced by the more pragmatic leadership that came to power in December 1986 under Party Secretary Nguyen Van Linh. [redacted] 25X1

The law supercedes a 1977 government decree which, by Hanoi's account, failed to attract significant investment. More to the point, Western countries cut off aid and credit to Vietnam following its invasion of Cambodia in 1978. Reports indicate that businessmen, especially the Japanese, have remained interested in Vietnam nevertheless because of its low-cost, highly disciplined labor force, its good location as an export base, and its large domestic market of 63 million. [redacted] 25X1

Highlights of the New Law

The code allows three forms of foreign investment: wholly foreign-owned enterprises, joint ventures in which foreigners provide up to 99-percent equity, and contract joint ventures in which Vietnamese and foreign partners cooperate without forming an enterprise, such as a recently announced fishing agreement with a private Thai firm. A state commission for foreign investment will be created to provide one-stop problem solving by cutting through the bureaucracy. Foreign investors will also be able to have disputes settled by third-country arbitration. All areas of the economy except defense and public utilities would be open for investment. According to press reports, Hanoi is particularly interested in encouraging foreign investment in:

- Export and import substitution industries.
- Industries using high technology and skilled labor.
- Industries that do not require expensive imported inputs.
- Services, such as tourism, that earn foreign exchange. [redacted] 25X1

Joint ventures and foreign-owned enterprises are to be taxed at 15 to 25 percent of earned profits, but certain joint ventures may be exempted for up to two years. Taxes will be higher for companies dealing in petroleum, natural gas, and other valuable resources. Joint ventures will in principle be allowed unlimited access to the domestic Vietnamese market and permitted to repatriate profits after paying an additional tax of between 5 and 10 percent. Our initial analysis shows that the code's provisions are fairly liberal for a Communist country and is very similar to China's code (see Appendix B). [redacted] 25X1

[redacted] 25X1

The Code's Impact

Although the code clears away some obstacles to investment, several details remain that, in our view, will prevent any substantial influx of Western investment. For example, in the case of joint ventures, the law circumscribes investors' decisionmaking powers by stipulating that either the general director or the first deputy director of the management board be a Vietnamese citizen. In addition, the management board must decide "important matters" on the principle of unanimity. The code actually discourages joint ventures from entering the Vietnamese market by requiring them to generate foreign exchange to repatriate profits. Furthermore, implementation of the code will take time. According to press reports, Hanoi does not expect all of the code's provisions to be in effect until the end of 1988 at the earliest. [redacted] 25X1

Other factors will, in our view, also discourage foreign investment. Foreign firms operating in Vietnam, such as Japan's Mitsubishi and Nissho Iwai Corporations complain about the rigid bureaucracy and argue that Vietnamese companies often back out of contracts or fail to meet deadlines, according to press reports. They are also critical of the weak banking system and poor infrastructure. Many interested firms are likely to hold off to see how other companies do under the new law. Finally, most foreign governments probably will continue to discourage firms from investing in Vietnam until Hanoi's troops leave Cambodia. [redacted] 25X1

For its part, Hanoi is trying to exploit growing international interest in possible commercial opportunities. Hanoi recently claimed that France was planning to lend Vietnam $40 million to pay foreign debts, but we have no evidence of this. We believe Hanoi is deliberately overstating its economic dealings with France to encourage other Western countries to enter into business arrangements. Also, according to Hanoi, a number of foreign oil companies are eagerly seeking to negotiate for petroleum concessions in Vietnam, citing the new investment code, the tax advantages offered, and low production costs as reasons for heightened interest. [redacted] 25X1

This type of pitch was recently made by Vietnamese officials in Thailand and Singapore who stressed the opportunities under the new investment code. According to the US Embassy in Bangkok, the Vietnamese intend to tout the code in Australia and Japan after leaving Thailand. In Singapore, [redacted] the 25X1
Vietnamese tried to drum up investor interest in oil refining and shipbuilding, activities that Singapore specializes in. Vietnamese officials, probably inspired by overly optimistic promises of businessmen, have been exaggerating the prospects for South Korean investment in Vietnam. [redacted] 25X1
the Vietnamese claim that the South Korean firm Samsung has built several television plants in Vietnam. According to the US Embassy, the South Korean Foreign Ministry flatly denies the claim, but acknowledges that discussions on such investment in Vietnam are under way. [redacted] 25X1

[redacted] 25X1

Appendix A

Present Economic Conditions

Vietnam, one of the world's poorest nations, has chronic and severe economic problems. Per capita income ranks among the world's lowest, ranging between $150 and $200 per year. Inflation is running at an annual rate of about 1,000 percent. Vietnamese economists estimate that over a million people enter the work force every year, with less than half finding full-time jobs. The government budget has been crippled by costly food subsidies, and the leadership concedes that the economy is dependent on the annual $2-3 billion of Soviet economic and military aid, which officials admit has been wasted on large, inefficient, heavy-industrial projects while vital small-scale industries and agriculture have gone unfunded. According to official statistics, economic growth in 1985-86 slowed to an average of 5 percent, compared with an average annual growth rate of 7 percent from 1981-84, but we believe these growth rates are seriously overstated. [redacted] 25X1

Official statistics indicate that growth in industrial output has slipped in recent years. Vietnamese industries are operating at about 50 percent of capacity, according to press reports. Industries lack raw materials, fuels, and water. Industrial production also suffers from transportation bottlenecks, inappropriate pricing policies, and a lack of managerial skills. The Vietnamese are unable to maintain their machinery because of parts shortages. [redacted] 25X1

The agricultural sector, the economy's success story during the early 1980s, is also experiencing hard times. Agricultural productivity is low because the country lacks insecticides, fertilizers, and farm machinery. Grain production--which rose from 12 million to 18 million tons from 1979-85--is leveling off, and last year's insect-damaged crop failed to meet the government's target for the third straight year. Hanoi is especially worried because agriculture has to generate jobs and feed the country's rapidly growing population, which is expanding 2.5 percent a year and could reach almost 90 million by the year 2000. [redacted] 25X1

Vietnam does not have the foreign exchange or the creditworthiness to make needed investment in agriculture and to import equipment and spare parts to upgrade the country's antiquated factories. After selling a substantial portion of its gold reserves in the past few years, Hanoi has seen its hard currency reserves drop to roughly $10 million, or about three days' worth of imports, according to the IMF. Moreover, with exports largely limited to agricultural products and handicraft items, Vietnam's ability to generate foreign exchange is poor. [redacted] 25X1

[redacted] 25X1

Appendix B

Vietnam-China: A Comparison of Foreign Investment Codes

Many of Vietnam's economic reforms are patterned after China's and the new foreign investment code is no exception. Both Hanoi and Beijing's investment laws offer third country arbitration of disputes, guarantees against nationalization, and encourage joint ventures to give preference to domestic inputs whenever possible. Some subtle differences include:

Provision	China	Vietnam
Minimum contribution by foreign participant in a joint venture.	25 percent.	30 percent.
Taxes.	High technology firms may apply for a reduction or exemption from income taxes the first two or three years. Foreign participants who reinvest profits may apply for partial restitution of taxes.	Taxes may be deferred for up to two years after a venture begins and reduced by 50 percent for the subsequent two years. Reinvested profits are exempt from taxes or taxed at a reduced rate.
Investment contract length and extension option.	Length determined by parties involved. May be extended	Normal length up to 20 years. May be extended.
Management of joint ventures.	Composition of board of directors stipulated in the contract. Board chairman must be a Chinese citizen with one or two vice chairmen appointed by foreign participant.	General director or first deputy director must be Vietnamese citizen. Management board must decide key issues on the principle of unanimity.

[redacted] 25X1

Repatriation of profits.	**Profits may be remitted abroad after executing legal obligations and meeting Bank of China foreign exchange regulations.**	**Profits may be remitted abroad if currency is the same used in the original investment and investors must also pay an additional tax of 5 to 10 percent.**

[redacted] 25X1

[redacted] 25X1

[redacted] 25X1

VIETNAM: BANKING ON NEW LAW TO ATTRACT WESTERN INVESTORS [redacted] 25X1

DISTRIBUTION:

NATIONAL SECURITY COUNCIL

1 - LTGEN COLIN L. POWELL, ASSISTANT TO THE PRESIDENT FOR NATIONAL SECURITY AFFAIRS, RM 493,
1 - JAMES A. KELLY, SENIOR STAFF MEMBER EAST ASIA, RM 493,
1 - RICHARD CHILDRESS, DIRECTOR OF ASIAN AFFAIRS RM 392,

DEPARTMENT OF STATE

1 - WILLIAM CLARK JR, DEPUTY ASSISTANT SECRETARY RM 6205,
1 - DAVID LAMBERTSON, DEPUTY ASSISTANT SECRETARY FOR EAST ASIAN AND PACIFIC AFFAIRS, RM 6205,
1 - VICTOR TOMSETH, DIRECTOR, OFFICE OF THAILAND & BURMA AFFAIRS, RM 5206,
1 - WILLIAM DAVNIE, OFFICE FOR E. ASIA AND PACIFIC SOUTHEAST ASIA DIVISION, RM 8647,
1 - DOROTHY AVERY, OFFICE FOR E. ASIA AND PACIFIC SOUTHEAST ASIA DIVISION, RM 8647,
1 - PAULA CAUSEY, OFFICE OF ANALYSIS FOR E. ASIA AND PACIFIC/SA, RM 8647,
1 - RANDALL ELLIOTT, OFFICE OF POLITICO-MILITARY ANALYSIS/GPT, RM 6510A,
1 - DIRECTOR, OFFICE FOR INDONESIA, MALAYSIA, BRUNEI, AND SINGAPORE AFFAIRS, RM 5206,
1 - RENA EPSTEIN, POLICY PLANNING STAFF RM 7316,

DEPARTMENT OF DEFENSE

1 - COL CONRAD BELATEUR, US EMBASSY J5 FESA, RM 2E973,
1 - JOHN J. SLOAN, DEFENSE INTELLIGENCE OFFICER, EAST ASIA AND PACIFIC, RM 2C238,
1 - GORDON BARE, ASST. FOR THAI, BURMA, VIETNAM, LAOS, AND CAMBODIA OSA/ISA/EAPR, RM 4C839,
1 - LTCOL EDWARD HAYDASH, HQDA (DAMI-FII) RM 2A474,
1 - MAJ FRANCIS DONG, USA, J5 FESA RM 2E973,
1 - LTCOL WILLIAM WISE, ASSISTANT FOR REGIONAL POLICY AND CONGRESSIONAL AFFAIRS, RM 4C839,
1 - KARL D JACKSON, DAS OF DEFENSE, PACIFIC AFFAIRS, ISA, RM 4E816,
1 - LTCOL JAMES R. WILLIAMS, THAILAND, BURMA, VIETNAM, LAOS AND CAMBODIA DESK OFFICER, RM,

[redacted] 25X1

[redacted] 25X1

DEFENSE INTELLIGENCE AGENCY

1 – [redacted] DIA RM DB4E2, 25X1
1 – DIA/DB-2C1 DIAC, RM DB4E2,
1 – [redacted] DIA/DB-2C4 DIAC, RM C245A, 25X1
1 – [redacted] DIA/DE-2 DIAC, RM B6828,
1 – [redacted] DIA/AT-3 PLAZA WEST, RM 1120,
1 – [redacted] DIA/DE2 DIAC, RM B6-823,
1 – [redacted] JSI-3B RM 1C938B,
1 – [redacted] DIAC RM DB-2,

DEPARTMENT OF COMMERCE

1 – RANDALL FORT, SPECIAL ASSISTANT TO SECRETARY NATIONAL SECURITY, RM 2049
1 – [redacted] 25X1
2 – [redacted]
1 – BETSY HUDSON, RM 6854,

DEPARTMENT OF ENERGY

1 – LONNA EKIMOFF, RM 7G090,

FEDERAL RESERVE BOARD

1 – ROBERT EMERY, FEDERAL RESERVE BOARD RM B-1266,

CENTRAL INTELLIGENCE AGENCY

1 – [redacted] OFFICE OF EAST ASIAN ANALYSIS CHINA DIVISION, RM 4G20, 25X1
1 – RESEARCH DIRECTOR, OFFICE OF EAST ASIAN ANALYSIS RM 4F18,
1 – ANALYTIC GROUP, NATIONAL INTELLIGENCE COUNCIL RM 7E47,
1 – DIRECTOR, OFFICE OF EAST ASIAN ANALYSIS RM 4F18,
1 – DDI, RM 7E44,
1 – SENIOR REVIEW PANEL, RM 7B42,
1 – PRESIDENT'S, DAILY BRIEF STAFF RM 7F30,
1 – EA, NATIONAL INTELLIGENCE OFFICER RM 7E62,
1 – CHIEF, EA/[redacted] RM 5D00, 25X1
1 – INTELL.SUPPORT STAFF, OFFICE OF CURRENT PRODUCTION & ANALYTIC SUPPORT, RM 7G50,
6 – CONTROL BRANCH, OFFICE OF CURRENT PRODUCTION & ANALYTIC SUPPORT, IMC, RM 7G07,

[redacted] 25X1

[redacted] 25X1

1 – SPEC ASSIST DISSEM ANAL, OFFICE OF CURRENT PRODUCTION & ANALYTIC SUPPORT, RM 7G50,
1 – DIRECTOR, DCI/DDCI, EXECUTIVE STAFF, RM 7E12,
1 – DDO, RM 7E22,
1 – CHIEF, PRODUCT EVALUATION STAFF RM 2G25,
1 – DIRECTOR, LDA/EA RM 1H18,
1 – PRODUCTION OFFICER, OFFICE OF EAST ASIAN ANALYSIS RM 4G48,
1 – [redacted] SOUTHEAST ASIAN ISLANDS BRANCH, RM 4F38, 25X1
10 – [redacted] SOUTHEAST ASIA INDOCHINA, THAILAND, MALAYSIA, RM 4F24,
1 – [redacted] OFFICE OF EAST ASIAN ANALYSIS SOUTHEAST ASIA DIVISION, RM 4F38, 25X1
1 – DEPUTY CHIEF, OFFICE OF EAST ASIAN ANALYSIS SOUTHEAST ASIA DIVISION, RM 4F38,
1 – CHIEF, OFFICE OF EAST ASIAN ANALYSIS NORTHEAST ASIA DIVISION, RM 4G43,
1 – CHAIRMAN, NATIONAL INTELLIGENCE COUNCIL RM 7E62,
1 – DDO, EAST ASIA DIVISION [redacted] RM 5C18, 25X1
1 – [redacted]
1 –
1 –
1 –
1 –
1 –
1 –
1 – CHIEF, OFFICE OF GLOBAL ISSUES RESOURCE ANALYSIS BRANCH, RM 3G31,
[redacted] 25X1

[redacted] 25X1